

**SUBMISSION TO THE
INTERNAL REVENUE SERVICE
UNDER THE TAX WHISTLEBLOWER ACT,
26 U.S.C. § 7623(b)**

**REGARDING
UNDERREPORTING OF LOBBYING AND OPERATION IN FURTHERANCE OF
PRIVATE CORPORATE INTERESTS
IN CONTRAVENTION OF 26 U.S.C. § 501(c)(3)
TAX-EXEMPT CHARITABLE STATUS
IRS REFERENCE NO. [PENDING]**

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Eric R. Havian
Erika A. Kelton
PHILLIPS & COHEN LLP

131 Steuart Street, Suite 501
San Francisco, CA 94105
Tel: (415) 836-9000
Fax: (415) 836-9001

INTRODUCTION

This submission is made pursuant to the whistleblower provisions of 26 U.S.C. 7623 *et seq.* (the “Tax Whistleblower Act”). This matter concerns the massive underreporting of lobbying by the American Legislative Exchange Council (“ALEC”). While ostensibly a non-profit organization under Section 501(c)(3) of the Internal Revenue Code, ALEC’s primary purpose is to provide a vehicle for its corporate members to lobby state legislators and to deduct the costs of such efforts as charitable contributions. ALEC drafts “model” legislation provided by its corporate and legislative members, and lobbies for the adoption of that legislation. These goals are fundamentally inconsistent with ALEC’s claimed tax-exempt status as a charitable organization under 26 U.S.C. § 501(c)(3), because (i) “no substantial part” of a charity’s activity can be “attempting to influence legislation,” and (ii) ALEC’s activities do not qualify under any of the enumerated purposes of Section 501(c)(3).

This scheme causes harm to taxpayers in two distinct ways. First, ALEC’s activities constitute an abuse of its 501(c)(3) tax exemption, which is reserved for organizations “operated exclusively” for a limited number of purposes, such as “religious, charitable, scientific … or educational purposes” 26 U.S.C. § 501(c)(3). Second, ALEC’s corporate members improperly deduct from their taxable income the dues and other contributions made to ALEC; such expenditures are non-deductible lobbying expenses under Section 162(e). In fact, because ALEC solicits very few contributions from individuals, its false claims of tax-exempt status appear driven by the desire of ALEC corporate members to deduct lobbying expenses as charitable contributions.

ALEC's primary, if not sole objective is to "influence legislation." Its bylaws state that its purpose is to "formulate legislative action programs," "disseminate model legislation and promote the introduction of companion bills in Congress and state legislatures," and "[e]stablish a clearinghouse for bills at the state level, and provide for a bill exchange program."¹ As recently as April 11, 2012, ALEC boasted that "for years, ALEC has partnered with legislators to research and develop better, more effective ... legislation."² Notwithstanding these claims, however, ALEC has reported "for years" to the IRS that it has not spent a single penny on lobbying or attempting to influence legislation. These tax returns are patently false.

ALEC is a de facto organization of corporations, which have veto power over any ALEC legislation, and which pay enormous sums of money for the privilege of lobbying ALEC's legislator-members (who pay nominal dues of \$50 per year). ALEC spends its resources enabling its corporate members to communicate their desired legislative outcomes to state lawmakers, publicly brags that it "partner[s]" with legislators to pass the so-called "free-enterprise" corporate-drafted bills into law, but disclaims in its IRS 501(c)(3) filings that it spends resources on attempting to influence legislation. ALEC is a corporate lobbying group masquerading as a public charity.

The attached documents indicate the breadth of ALEC's efforts to influence legislation at the state level, and show direct efforts to lobby elected officials:

- **Issue Alerts** [Exhibit 1]: Email communications from ALEC to state legislators, titled "Issue Alerts," express ALEC's support for or opposition to policies and specific legislation. These communications from ALEC to state legislators reference

¹ American Legislative Exchange Council Bylaws, Article II, Year Ended December 31, 2007, <http://www.guidestar.org/FinDocuments/2007/520/140/2007-520140979-04559ea0-9.pdf>.

² Statement by ALEC, April 11, 2012, <http://www.alec.org/2012/04/alec-responds/>.

specific state bills and often include commentary comparing (favorably or unfavorably) the state legislation to an ALEC bill that is “approved” by one of its nine “Task Forces.” Each Task Force is made up entirely of ALEC members: state legislators and representatives from dues-paying private corporate businesses and other organizations. In practice, ALEC-approved bills are those desired by ALEC’s private sector members, who have ultimate control over them. The issue alerts plainly are an attempt to “influence legislation.”

- **ALEC Talking Points [Exhibit 2]:** ALEC provides what it calls “talking points” to state legislators, tailored to specific state legislative bills, as well as talking points about broad policy areas. ALEC describes at least one set of talking points as being “designed to help you navigate away from . . . tough questions,” including those “from the press and from state legislative committees.” ALEC then lists what it calls “acceptable responses” to the “tough questions” about whether ALEC lobbies, where it receives its funding, why its staff is not registered as lobbyists, and ALEC’s participation in the Koch Associates program. For example, ALEC’s talking points propose that one “tough question” might be “[w]ith over 1,800 legislative members, I’d say that they definitely have the biggest voice.”
- **ALEC Model Press Releases [Exhibit 3]:** ALEC provides boilerplate press releases to legislators that the legislators are encouraged to modify when the legislature

introduces or passes one of ALEC’s bills, in a further attempt to “influence legislation.”

- **ALEC Task Force Materials [Exhibit 4]:** ALEC administers the operation of nine Task Forces. Each Task Force is made up of state legislators and representatives from private corporations. The Task Forces approve ALEC’s bills, which are then largely copied and introduced in state legislatures. The attached Task Force materials identify individuals and corporations responsible for the proposed statutory language. These materials include agendas, minutes and the corporate and legislator membership lists of various Task Forces. The Task Forces are no more than a forum for ALEC’s corporate members to lobby its legislator members.
- **ALEC bill tracking documents [Exhibit 5]:** ALEC spends resources preparing and researching the legislative process in anticipation (and as a result) of its lobbying. ALEC tracks its approved legislation when it is introduced in state legislatures, and makes contacts with state legislators about the bills. ALEC’s spreadsheets identify where legislators have introduced bills substantially similar to ALEC legislation. The tracking documents include specific details about the bills (for example, the bill number and its sponsor) and their status. The sole purpose of this bill tracking and communication with legislators is to “influence legislation.”
- **ALEC hearing testimony [Exhibit 6]:** ALEC staff frequently testify in support of bills relating to their own model legislation, appearing before statehouse committee hearings, or by providing written comments for consideration, a core function of “influencing legislation.”

Pursuant to the Tax Whistleblower Act, we respectfully request that the IRS investigate ALEC's previous submissions to the IRS, in which it certifies that it does not spend any money on lobbying. Moreover, the IRS should investigate whether ALEC operates in contravention of its Section 501(c)(3) status, because it does not operate "exclusively" for charitable and educational purposes, but instead operates to advance private business interests. Finally, the IRS should disallow the tax deductions taken by ALEC's for-profit corporate members, and collect taxes due from such members.

A. THE AMERICAN LEGISLATIVE EXCHANGE COUNCIL (ALEC)

The American Legislative Exchange Council ("ALEC"), incorporated in the state of Illinois in 1974, is a United States nonprofit corporation recognized by the Service as exempt from federal income taxation under Code section 501(c)(3).

As stated above, ALEC's bylaws provide that its purpose is to "formulate legislative action programs," "disseminate model legislation and promote the introduction of companion bills in Congress and state legislatures," and "[e]stablish a clearinghouse for bills at the state level, and provide for a bill exchange program."³ ALEC's mission statement describes that its goal is "*to advance the Jeffersonian principles of free markets, limited government, federalism, and individual liberty through a non-partisan, public-private partnership between America's state legislators and concerned members of the private sector, the federal government and the general public.*"⁴ ALEC explains that this mission "unites members of the public and private sectors in a dynamic partnership to support research, policy development, and dissemination

³ American Legislative Exchange Council Bylaws, Article II, Year Ended December 31, 2007, <http://www.guidestar.org/FinDocuments/2007/520/140/2007-520140979-04559ea0-9.pdf>.

⁴ ALEC Form 990 for Year 2009.

activities” when it “enlist[s] state legislators from all parties and members of the private sector who share ALEC’s mission.”⁵

ALEC is governed by a Board of Directors consisting of incumbent state legislators. ALEC has a second parallel “Private Enterprise Board,” whose duties include the critical task of selection of the private sector members of each of the ALEC Task Forces, and also the private sector Task Force chairs. *See Part VI-D of [Exhibit 7].*

ALEC offers two forms of membership: Legislative and Private Sector. Legislative members are incumbent state legislators who pay \$100 for a two-year membership. Private sector (or corporate) members pay a minimum of \$7000 for annual membership in ALEC, plus substantial additional fees to become a member of one or more of ALEC’s nine task forces. Corporate members also make contributions to ALEC for various other purposes. It appears likely that these private corporate members deduct ALEC dues and contributions from their taxable income.

Although its governing board is composed of legislators, ALEC is effectively controlled by its corporate members, which provide the bulk of ALEC’s funding and retain veto power over all ALEC legislation and policy statements. In fact, at the present time it appears that the reason for ALEC’s existence, and for its dubious claim to tax-exempt status, is to provide these corporate interests with a forum in which they can undertake taxpayer-subsidized lobbying in support of their goals. Because ALEC does not solicit a substantial portion of its funding from individual donors, the financial benefit of its 501(c)(3) status flows to corporate donors, who can deduct what would otherwise be unallowable lobbying expenses.

⁵ About ALEC, <http://www.alec.org/about-alec/> (last accessed April 13, 2012).

B. LEGAL STANDARDS FOR LOBBYING ACTIVITY

ALEC qualifies as a Section 501(c)(3) organization only if “no substantial part of [its activities] is carrying on propaganda, or otherwise attempting, to influence legislation (except as otherwise provided in subsection (h)).” The Code creates two alternative tests that define the maximum resources that a charity may devote to lobbying. The default is simply the “no substantial part” test, which is not further defined. A charity may elect, however, to have its lobbying measured by the § 501(h) test. The election must be made in the year in which the charity intends to invoke the alternative test. 26 U.S.C. § 501(h)(6) & (7). It is unclear whether ALEC has made such an election, but under either test a substantial portion of ALEC’s activities constitute lobbying.

If ALEC has made an election under Section 501(h), that provision and Section 4911 would place a strictly defined limit on the amount of money ALEC could spend influencing legislation through direct lobbying (approximately 5% of its expenditures) and grass roots lobbying (approximately 1.25% of expenditures). 26 U.S.C. § 4911(c). Communications between ALEC staff and legislators referring to specific legislation and expressing ALEC’s support or opposition (its “view” on the legislation) would count as a lobbying expenditure. Treas. Reg. §§ 56.4911-2(b)(1)(ii) & 2(d)(1)(ii). If ALEC exceeds these strict limits on lobbying, it is subject to an excise tax, and could lose its exemption if it “normally” exceeds either lobbying limit by more than 50%.

Alternatively, ALEC could forego the bright line limits of Sections 501(h) and 4911, and instead rely on the statutory language that “no substantial part” of its activities is attempting to influence legislation. The regulations state that an organization attempts to influence legislation if it “[a]dvocates the adoption or rejection of legislation.” Treas. Reg. § 1.501(c)(3)-

1(c)(3)(ii)(b). Whereas the Section 501(h) test is measured by expenditures, the “no substantial part” is measured by “activities.”

C. ALEC LOBBIES AND SEEKS TO INFLUENCE LEGISLATION

ALEC disclaims any lobbying in its Form 990 tax returns, and it appears not to have made an election to have its lobbying expenses measured under section 501(h). Prior to 2008, Part VI-A of Schedule A to Form 990 was titled “Lobbying Expenditures by Electing Public Charities.” That Part stated that it was to be completed “ONLY by an eligible organization that filed Form 5768,” the Form required for an election under section 501(h). Page 10 of the Instructions also makes clear that this section must be completed by charities electing to have their lobbying measured by the alternative Section 501(h) test. ALEC’s returns for 2004 and 2007 state that Part VI-A is “Not Applicable,” and ALEC did not otherwise complete this section of the 2004 and 2007 returns. ALEC did complete Part VI-B, “For reporting only by organizations that did not complete Part VI-A.” It answered “No” to all questions regarding whether it “attempt[ed] to influence national, state or local legislation” [Exhibit 8] Thus, it appears from the 2004 and 2007 returns that ALEC did not elect 501(h) status.⁶

Form 990 was changed in 2008. In its returns for 2008-2010, ALEC answered “no” to Part IV, Question 4 (“Did the Organization engage in lobbying activities?”). Organizations that answer “yes” to this question must complete Schedule C, but ALEC’s return contains no Schedule C. These more recent returns also suggest, albeit not conclusively, that ALEC has not made a Section 501(h) election.

⁶ Inexplicably, ALEC’s returns for 2000-2003 and 2005-2006 are different from its 2004 and 2007 returns. For years other than 2004 and 2007, ALEC improperly filled out both Part VI-A and Part VI-B. It consistently represented, nonetheless, that it did no lobbying.

If, as suggested by its tax returns, ALEC has not elected to be governed by Section 501(h), its lobbying activity will be evaluated under the default test of Section 501(c)(3). That provision requires ALEC to demonstrate that it devotes “no substantial part” of its activities to attempting to “influence legislation.”

Under either test, the documents provided with this whistleblower submission show that ALEC is extensively involved in lobbying because its primary activities – including communications with legislators – are designed to influence the outcome of specific legislation, and because its basic practice is to contact state legislators to express its views on specific legislation. Those views reflect the positions of ALEC’s corporate “private sector” members that draft ALEC’s legislation alongside “public sector” lawmaker members. ALEC is explicit that it operates to “connect” state lawmakers with corporations to pass its agenda.⁷

Further, these documents show that ALEC’s lobbying greatly surpasses any amount that is permissible for a Section 501(c)(3) organization. This is because ALEC’s core activities, measured by its largest expenditures reported in its tax returns, are Task Force work and conferences for state legislators and corporations. In 2010, ALEC reported that it expended almost \$4 million on those activities (Form 990, Part III, Lines 4a and 4b) out of total expenditures of \$6 million (Part I, Line 18). [Exhibit 8] In ALEC’s words, its Task Forces and conferences allow its corporate members to “partner[] with legislators to … develop better, more effective … legislation.” *Id.* In other words, the Task Forces and conferences are forums for lobbying.

1. *Task Forces & ALEC Bills*

ALEC reports on its tax returns that its largest expenditures relate to the operation of its Task Forces. ALEC’s legislation is developed in advance of its scheduled Task Force meetings,

⁷ Statement by ALEC, April 11, 2012, <http://www.alec.org/2012/04/alec-responds/>.

which take place during the thrice yearly ALEC conferences. Here, ALEC's corporate members lobby its state legislator members, and agree on legislation that is stamped with ALEC's imprimatur.

Detailed "Task Force Operating Procedures" are included in every set of Task Force Materials distributed in advance of Task Force meetings, and strictly control operation of those meetings. The Procedures show the breadth of ALEC's work to influence legislation in each state. In these Procedures, ALEC describes its Task Forces as "forums for an exchange of ideas and sharing of experiences between ALEC's state legislator and private sector members." It then states that Task Forces are "responsible for developing and sponsoring" quintessential lobbying events, such as "issue specific briefings, press conferences and press campaigns" and "witness testimony and the activities of policy response teams." [Exhibit 7]

Each of ALEC's nine Task Forces⁸ is co-chaired by both a state legislator "public sector" ALEC member and a "private sector" ALEC member, with these individuals having shared responsibility for setting the agenda for task force meetings.⁹ Private sector members include representatives from major for-profit corporations, including AT&T, State Farm Insurance, Reynolds American and ExxonMobil Corporation.¹⁰ Both the public sector and private sector members propose legislation to be adopted as an ALEC bill. The ALEC bills propose statutory

⁸ The exhibits of this submission relate to nine of ALEC's Task Forces: Civil Justice; Commerce, Insurance, and Economic Development; Communications and Technology; Education; Energy, Environment, and Agriculture; Health and Human Services; International Relations; Public Safety and Elections; Tax and Fiscal Policy. On April 17, 2012, ALEC announced that it was shuttering its Public Safety and Elections Task Force and "reinvesting these resources in the task forces that focus on the economy." See ALEC Sharpens Focus on Jobs, Free Markets and Growth – Announces the End of the Task Force that Dealt with Non-Economic Issues. <http://www.alec.org/2012/04/alec-sharpens-focus-on-jobs-free-markets-and-growth-announces-the-end-of-the-task-force-that-dealt-with-non-economic-issues/>

⁹ ALEC Task Force Operating Procedures: III-General Procedures-A. See Exhibit 7

¹⁰ <http://www.alec.org/about-alec/private-enterprise-board>.

language for how ALEC's favored policies should best be codified under state law. ALEC's bills are used as model legislation in state legislatures across the country. [Exhibit 9]

ALEC's Task Forces utilize procedures that mimic the legislative process that its public sector members are accustomed to – ALEC's bills are “referred” to specific Task Forces for discussion among the corporate members and the state legislators, and then the Task Force members “pass” the bills out of the Task Force. Task Force members may also introduce “amendments” to ALEC's bills. Task Force participation is strictly controlled. While “[a]ll Task Force meetings are open to registered attendees . . . [o]nly regular Task Force Members may introduce any resolution, policy statement or model bill. Only Task Force members will be allowed to participate in the Task Force meeting discussions and be seated at the table . . . All Task Force and Executive Committee meetings shall be conducted under the guidelines of Roberts Rules of Order.” Most importantly for purposes of establishing corporate control over legislation, no bill or policy may be adopted without the concurrence of a majority of both private sector and public sector Task Force members. [Exhibit 7]

Documents attached as Exhibit 4 are ALEC Task Force Materials that are distributed in advance of these meetings. The enclosed Task Force materials include, among other documents:

- Tentative agendas identify the “public sector” (state legislator) and “private sector” (corporate representative) chairs for each Task Force, allot time for “Consideration of Model Legislation” that has already been “passed” by a Task Force, for discussion of amendments to ALEC's bills, and for “Consideration of Proposed Model Legislation” – which allows private sector and public sector members to introduce their preferred legislative language, open it to discussion, and “pass” the bill out of the Task Force;

- Draft ALEC legislation, detailing the name of the public or private sector sponsor;
- Draft amendments to ALEC legislation;
- Membership lists and contact information for public and private sector members of the task force;
- Minutes from previous Task Force meetings; and
- Articles of interest.

An example of an ALEC bill that resulted from this process is attached as Exhibit 10.

The language of this bill, known as the “Stand Your Ground” law, was originally drafted with the assistance of the National Rifle Association (“NRA”), an ALEC private sector member, for introduction in the Florida legislature, passing in April 2005.¹¹ The NRA then sponsored this bill at the ALEC Criminal Justice Task Force (later renamed Public Safety and Elections) in August 2005, and asked that it be adopted as an ALEC bill, which it was by unanimous vote of both the public and private sectors.¹² In response to a recent wave of resignations by ALEC private sector members, ALEC has discontinued this Task Force.

ALEC works to introduce its bills in state legislatures throughout the country, utilizing its network of dues-paying state legislators and corporations that authored and “passed” the bills out of each Task Force. As will be discussed more fully below, once the Task Forces approve model legislation, ALEC strategically deploys its resources to influence adoption of that legislation,

¹¹ Joe Strupp, “Former NRA President: We Helped Draft Florida’s ‘Stand Your Ground’ Law,” Media Matters for America Blog, March 27, 2012, <http://mediamatters.org/iphone/blog/201203270005>.

¹² NRA-ILA, Institute for Legislative Action, Legislation, August 12, 2005, <http://nraila.org/legislation/state-legislation/2005/8/nra-presents-alec-model-legislation-in.aspx?s=st=ps>.

utilizing various lobbying tools, including model talking points, model press releases, and commentary on specific state legislation in the “issue alerts” it distributes to state legislators.

ALEC boasts about how frequently its bills are introduced in state legislatures to show its influence over the legislative process, publishing “scorecards” to demonstrate the high numbers of ALEC bills enacted. [Exhibit 9] In its 1995 scorecard, then-ALEC Executive Director Samuel A. Brunelli explicitly stated that corporations join ALEC to drive a legislative agenda in a cost effective way: **“This was a landmark legislative year in ALEC’s history,’ said ALEC Executive Director Samuel A. Brunelli. ‘With our success rate at more than 20 percent, I would say that ALEC is a good investment. Nowhere else can you get a return that high.”** [Exhibit 11] Similarly, in a brochure that ALEC distributed to recruit more corporations for its private sector membership, it claimed that “during each legislative cycle, ALEC legislators introduce more than 1,000 pieces of legislation based on these models, approximately 17 percent of which are enacted.” [Exhibit 12] It is telling that ALEC expresses its success in corporate terms, as a good “return” on a corporation’s “investment” in tax-exempt lobbying.

Beyond quantifying its influence by measuring how often its lobbying efforts succeed, ALEC trumpets how its Task Forces and other programs provide corporations with direct access to state legislators. In a near textbook definition of lobbying, the recruitment brochure states “ALEC provides the private sector with an unparalleled opportunity to have its voice heard, and its perspective appreciated, by the legislative members.” *Id.* The brochure further explains that “[t]his partnership identifies issues and then responds with common-sense, result-oriented policies. The two groups work in unison to solve the challenges facing the nation, with results that will define the American political landscape in the 21st century.” *Id.* In other words, ALEC provides a network to influence the legislative process and deliver “results” to its private

corporate membership – namely, legislation favorable to corporate members’ interests. These statements by ALEC belie any claim that it is engaged in “education” rather than lobbying. The ALEC Task Forces provide a venue for corporations to lobby legislators while deducting the expenses as charitable donations.

2. *Issue Alerts and Related Lobbying Contacts*

Once a Task Force passes an ALEC bill, ALEC deploys resources to strategically target the legislative process as it monitors state legislation. ALEC staff regularly distributes “Issue Alerts” via email to state legislators nationwide, specifically comparing state legislation to its model bills, and expressing “support for the policies” in the state legislation. Issue Alerts are attached as Exhibit 1. Usually, the Issue Alert cites a specific state bill by its title and number, and then expresses support for or opposition to the bill’s policies. ALEC also communicates its view on specific legislation directly to state lawmakers. Sometimes ALEC uses these “Issue Alerts” to express support for the adoption or defeat of proposed amendments to the state legislation. These Issue Alerts constitute direct evidence of ALEC’s lobbying because they are communications that are clearly targeted to influence legislation and disclose ALEC’s view on the legislation.

Other times, ALEC’s lobbying is even more strategic. For example, ALEC’s staff will directly contact state legislators on a one-on-one basis to advocate for specific ALEC bills. On January 21, 2011, one of ALEC’s Task Force Directors (based in ALEC’s Washington, D.C. headquarters) emailed an Ohio state legislator, stating that he “heard that you might be considering ALEC’s Private Attorney Retention Sunshine Act for Ohio. Wonderful to hear. If you need any of ALEC’s help or need any information while you are considering the legislation, don’t hesitate to ask!” [Exhibit 13] In another email, an ALEC Task Force Director emailed an

Ohio State Senator, explicitly stating that ALEC is “encouraging as many states as possible to consider the Private Attorney Retention Sunshine Act legislation” and that “[s]o far, 10 states have introduced bills. No pressure, but I thought I would email you the bill and a discussion piece in case you are interested in introducing the bill in Ohio.” [Exhibit 14] These emails speak for themselves – they are directed at specific legislators to influence the outcome of particular state legislation. In another email, dated July 6, 2009, ALEC asked members to sign on to a letter opposing specific aspects of then-pending federal health care reform legislation. The letter was addressed to Senator Robert Byrd and Speaker Nancy Pelosi and copied to multiple other Congressional leaders. [Exhibit 15] There is no doubt this exercise represents an attempt to influence legislation.

3. *ALEC Bill Tracking Documents*

ALEC works to track its bills as they are used to formulate state legislation. Exhibit 5 is a group of “ALEC State Tracking” spreadsheets for what ALEC calls its “good bills” and “problematic bills” from its Civil Justice and Energy, Environment & Agriculture Task Forces. When ALEC boasts about how frequently its legislation becomes law, these tracking documents show how ALEC is able to corroborate its effectiveness at lobbying. They show the state legislation and the comparable ALEC bill by title. These documents guide ALEC as it communicates its views on specific legislation.

For example, ALEC’s Civil Justice Task Force tracked 50 “problematic bills” indicating ALEC’s opposition. One bill, Ohio bill SB143 (Damages for Fraud Act), would enable the state of Ohio to recover fraudulent charges from contractors. Exhibit 16 is a memo sent May 6, 2011 from Ohio Senator Seitz to ALEC’s Ohio legislative chair John Adams, discussing ALEC’s opposition to the bill. This is an example of ALEC expressing its views on the legislation, in

furtherance of its agenda. The state senator wrote that “[w]hile this is understandable as states are broke, the considered advice from our friends at ALEC was that such legislation is not well taken and should not be approved.”

4. *Model Press Releases & Talking Points*

Exhibits 2 and 3 show ALEC’s efforts to frame media coverage of its favored legislation. Exhibit 3 is a collection of model press releases that may be modified by state legislators concerning ALEC’s activities. ALEC also provides legislators with model “Talking Points” designed to assist state legislators with specific policy and bills, so that legislators are prepared to talk to their colleagues and the media about proposed legislation. These materials are unquestionably for the purpose of influencing legislation.

5. *ALEC Conferences*

ALEC’s conferences are held three times annually, at locations across the United States, typically in luxury hotel resorts. Legislators are actively encouraged to bring their families, with subsidized child care provided by ALEC, called “ALEC Kids Congress,” at a cost to ALEC of \$251,873 in 2009 according to IRS filings. [Exhibit 8]

Conferences are attended by both ALEC’s public and private sector members. The agenda consists of large plenary sessions, Task Force meetings, evening events and receptions. Private sector members co-organize numerous sponsored events with ALEC staff, including the National Rifle Association’s annual clay pigeon shooting event. Other events at the 2011 ALEC Annual Meeting included a Cigar Reception sponsored by Reynolds Tobacco and the Cigar Association of America, and an evening of dancing with food and refreshments sponsored by Cox. [Exhibit 17] These events are promoted ahead of the conference by ALEC staff via email

to legislators. It is likely that the corporations that pay for such lavish lobbying junkets deduct the expenses as charitable contributions to a 501(c)(3) organization.

Legislator members on ALEC Task Forces are also eligible for “ALEC scholarships,” which reimburse a legislator’s accommodation, transportation and other expenses to attend the ALEC national conferences. Scholarships are also available for legislators to attend other events, including “ALEC Academies,” which are described as a “two-day intensive program on a specific issue,” attended by invited members of both the public and private sector. Contributions to the ALEC scholarship fund are made by corporations who are solicited directly by legislators at the individual state level. *See Exhibit 18* (a breakdown of payments to the ALEC in Ohio scholarship fund). According to the tax filings of PhRMA, the pharmaceutical lobbying group and ALEC private sector member, it provided \$356,075 to the ALEC scholarship fund in 2010.¹³ Many of these expenses are likely deducted from corporate taxable income.

The ALEC conferences are nothing more than a forum for tax-subsidized lobbying. ALEC provides logistical support in the form of travel, accommodations, entertainment, and family services, in order to facilitate lobbying by ALEC’s corporate members targeting ALEC’s legislative members.

6. *ALEC hearing testimony*

ALEC also influences legislation through hearing testimony. Exhibit 6 includes examples of such testimony, where ALEC is often on record as it, in ALEC’s words, “applauds” specific bills and explains whether it supports specific provisions. ALEC staff routinely appears before legislative committees to communicate with legislators about ALEC’s views on legislation to influence the outcome of specific bills. Like nearly all of ALEC’s core activities, the hearing testimony constitutes paradigmatic lobbying.

¹³ <http://www.prwatch.org/node/11342>.

D. ALEC's LOBBYING DOES NOT CONSTITUTE "COMMUNICATION WITH MEMBERS"

ALEC may try to argue that at least some of its communications are excluded from the definition of lobbying under the special rules for communications with organization membership. Under Section 501(h), an organization that makes an election to be covered by that subdivision may rely on a definition of "lobbying" that excludes communications with the organization's own members, if the communication concerns legislation that is of direct interest to the organization, and the communication does not directly encourage the member to engage in direct or grass roots lobbying. I.R.C. §§ 501(h) & 4911(d)(3); Treas. Reg. § 56.4911-5(b). This exception does not apply to ALEC for several reasons.

By its express terms Section 501(h) applies only to an organization "which has elected (in such a manner and at such time as the Secretary may prescribe) to have the provisions of this subsection apply to such organization" Section 501(h)(3). An election is only effective for years that "end after the date the election is made" Section 501(h)(6). For any year in which such election has not been timely made, "nothing in this subsection [(h)] or in section 4911 [26 USCS § 4911] shall be construed to affect the interpretation of the phrase 'no substantial part of which is ... attempting to influence legislation' under subsection (c)(3)." 26 U.S.C. § 501(h)(7). Because ALEC's tax returns reflect that it has not made an election under Section 501(h), the "member communication" provisions do not apply to it.

Even if ALEC had properly made such an election, its activities would not qualify as communications with members. The exception only applies to communications the organization makes to its members as members, not when it targets them in their capacity as legislators. That interpretation is made clear by Examples 7 and 8 to Treas. Reg. § 56.4911-2(b)(4). Example 7 discusses a situation where an organization sends a newsletter to 10,000 nonmember subscribers,

including “Senator Doe,” reflecting the organization’s view of a pending bill. The regulation explains that this would not be lobbying “because the newsletter is sent to Senator Doe in her capacity as a subscriber rather than her capacity as a legislator.” Example 8 assumes these same facts, but adds that Senator Doe’s staff requests further information from the organization, and the organization sends a letter in response reflecting its view of a specific bill. The organization’s letter “is a direct lobbying communication,” because the letter communicates with Senator Doe in her capacity as a legislator rather than as a “subscriber.”

Thus, the regulations expressly recognize that the capacity in which a legislator is engaged determines whether the communication is considered “lobbying.” It is irrelevant that a legislator happens also to be a “subscriber” (or in ALEC’s case, a “member”) if the communication is directed to that person in their legislative capacity. That is plainly the case with respect to communications between legislators and ALEC and/or its private corporate members. ALEC does not send Action Alerts and other communications to legislators simply to educate them about ALEC’s activities. It does so to encourage them, often explicitly, to introduce ALEC legislation and lobby for its passage.

Finally, if the IRS were to sanction ALEC’s scheme as mere communication with its members, it would open Section 501(c)(3) to unlimited abuse. Any lobbying organization could simply form a non-profit arm, invite legislators to join for a nominal membership fee, and conduct tax-exempt lobbying without any restrictions. Such an enormous loophole would eviscerate the lobbying exclusion of Section 501(c)(3) and open the floodgates to widespread abuse of tax-exempt activity.

E. ALEC’s ACTIVITY DOES NOT FALL WITHIN ANY OF THE PERMISSIBLE PURPOSES ALLOWED BY SECTION 501(C)(3)

Even if ALEC were not engaged in substantial “lobbying” within the meaning of the applicable regulations, it would still not be eligible for 501(c)(3) status. That is because ALEC’s activities, viewed as a whole, do not fall within any of the permissible purposes listed in that section.

Under Section 501(c)(3), an organization must be “operated exclusively” for one of the enumerated purposes. The only enumerated purpose even remotely applicable to ALEC would be “educational.” *See* Treas. Reg. § 1.501(c)(3)-1(d)(1). The regulations define “educational” as either instruction of individuals or “instruction of the public on subjects useful to the individual and beneficial to the community.” *Id.* at 1.501(c)(3)-1(d)(3). Moreover, while an educational charity may present a point of view, it must present “a sufficiently full and fair exposition of the pertinent facts as to permit an individual or the public to form an independent opinion or conclusion.” *Id.*

It is wildly implausible that ALEC’s “operations” are “exclusively” (or even primarily) devoted to “instruction of the public,” or that ALEC’s materials present a “full and fair exposition” of the issues. The documents we have provided clearly reflect that ALEC has no interest in “instruction of the public,” but is in the business of enacting legislation in which its corporate members typically have a pecuniary interest. Undoubtedly that is precisely how these for-profit companies justify to shareholders their large contributions to ALEC. Far from a “full and fair exposition,” ALEC’s materials present a one-sided view of its proposed legislation, complete with “talking points” and draft press releases. Contrast ALEC’s approach with other organizations that develop model legislation, most notably the National Conference of Commissioners on Uniform State Laws, which works through an open process, accepts members

from any ideological position, and generates work product that is publicly disseminated and includes detailed analysis and comment rather than just legislative text made available only to members who share a common ideology.

Thus, even if a tortured interpretation of the regulations led to the conclusion that ALEC is not engaged in lobbying, ALEC would fail to satisfy the most basic requirement for 501(c)(3) status – operations that are exclusively for charitable purposes. ALEC’s operations are neither charitable nor educational, much less exclusively so. They are pecuniary and political, and devoted to fostering the enactment of bills that will financially benefit and further the ideological goals of ALEC’s corporate membership. That is not a permissible activity for an organization that claims the privileges of a public charity.

CONCLUSION

ALEC reported to the Internal Revenue Service that it does not spend a penny on lobbying. However, ALEC’s own admissions in its tax returns about how much it spends on its Task Forces and Task Force meetings, coupled with the materials documenting communications between legislators and ALEC staffers about specific legislation, demonstrate that ALEC’s primary purpose is to influence legislation and advance the private legislative agenda of its corporate members. This is inconsistent with ALEC’s Section 501(c)(3) status, which requires that it be “exclusively” charitable and educational in purpose, and that “no substantial part of [its activities be] carrying on propaganda, or otherwise attempting, to influence legislation”

This whistleblower has produced extensive documents to show that ALEC’s core purpose is to influence legislation. The documents include voluminous evidence of direct lobbying communications with legislators expressing ALEC’s view on legislation. ALEC has grossly misrepresented its lobbying costs (by consistently reporting that it does *no* lobbying), and does

not operate within the limitations of 501(c)(3) status. Its own bylaws declare that its purpose is to “[d]isseminate model legislation and promote the introduction of companion bills in Congress and state legislatures” and “[f]ormulate legislative action programs.”¹⁴ As a consequence of ALEC’s improper assertion of 501(c)(3) status, its for-profit corporate members have improperly deducted their dues and other contributions to ALEC, despite the fact that such funds have been used for lobbying.

As a result, taxpayers have been damaged not only by ALEC’s abuse of a narrow tax exemption intended to facilitate the work of genuinely charitable organizations, but also by the loss of tax revenues from ALEC’s private corporate members, who are the primary if not exclusive beneficiaries of ALEC’s improper scheme. Accordingly, the IRS should conduct an immediate investigation, impose necessary penalties, and collect unpaid taxes for work done that is not consistent with ALEC’s tax-exempt charitable status.

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Eric R. Havian
Erika A. Kelton
Phillips & Cohen LLP
Attorneys for Robert W. Edgar

¹⁴ American Legislative Exchange Council Bylaws, Article II, Year Ended December 31, 2007, <http://www.guidestar.org/FinDocuments/2007/520/140/2007-520140979-04559ea0-9.pdf>.